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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Treatment of Local Exchange	)	CC Docket No. 92-101
Carrier Tariffs Implementing	)	
Statement of Financial	)	
Accounting Standards,	)	
"Employers Accounting for	)	
Postretirement Benefits Other	)	
Than Pensions"	)	

DIRECT CASE

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BELLSOUTH TELECOMMUNICATIONS, INC.

DATE: June 1, 1992

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APPENDIX

SUMMARY

In this Direct Case, BellSouth demonstrates that the incremental cost of OPEBs incurred by LECs as a result of adoption of SFAS-106 qualifies for exogenous cost treatment under the Commission's price cap rules.

SFAS-106 costs meet the Commission's definition of exogenous costs. These costs result from a change in GAAP rules that the Commission has ordered the LECs to adopt. These costs are not included in the initial price cap rates, and, as shown herein, only a minuscule amount of these costs may be recovered through any aspect of the price cap formula.

BellSouth has attached a study by Godwins, Inc. that demonstrates that only 0.7 percent of the cost of OPEBs borne by price cap LECs will be reflected in the GNP-PI. A macroeconomic model employed by Godwins demonstrates that price cap LECs may ultimately recover an additional 14.5 percent of its SFAS-106 costs through changes in national employment and wage rates. These changes will take place only over time. Therefore, a price cap LEC that seeks an exogenous cost adjustment of only 84.8 percent of its SFAS-106 costs in 1993 is clearly employing a conservative convention that will avoid double counting.

BellSouth has not yet adopted SFAS-106. In accordance with the Commission's instructions, BellSouth has provided a current, good faith estimate of its 1993 SFAS-106 costs in this Direct Case.

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In the Matter of	)	
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Treatment of Local Exchange Carrier Tariffs Implementing Statement of Financial Accounting Standards, "Employers Accounting for Postretirement Benefits Other Than Pensions"	)	CC Docket No. 92-101

DIRECT CASE

BellSouth Telecommunications, Inc. ("BellSouth") hereby files its Direct Case in the captioned proceeding, as required by the Commission's Order of Investigation and Suspension ("OIS") released April 30, 1992.[1]

As the Commission correctly states in the OIS, the Financial Accounting Standards Board adopted SFAS-106 in December, 1990. This standard mandates that businesses following Generally Accepted Accounting Principles ("GAAP") account for the cost of postretirement benefits other than pensions ("OPEBs") on an accrual basis rather than a "pay-as-you-go" basis for fiscal years beginning after December 15, 1992.[2] OPEBs consist primarily of medical benefits paid to retirees.

Under "pay-as-you-go" accounting, postretirement

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[1] BellSouth has not yet filed a tariff seeking to treat SFAS-106 costs as an "exogenous" adjustment to its price cap indices. In accordance with footnote 14 of the OIS, BellSouth submits in this direct case its current, good faith estimates of the impact of SFAS-106 on its costs.

[2] OIS at para. 2.

benefits are booked based on the amounts paid in the current accounting period for the benefit of retired employees. SFAS-106 requires that OPEBs be recognized as deferred compensation that is booked when the obligation to pay the benefits is earned by employees as they provide service to the employer. BellSouth's postretirement expenses are a combination of "pay-as-you-go" and contributions to Voluntary Employee Benefit Association ("VEBA") trusts. BellSouth has not yet adopted SFAS-106, but will do so on or before January 1, 1993.

The adoption of SFAS-106 has two immediate impacts: 1) a higher level of expense being recognized in the current accounting period; and 2) the creation of a transition obligation for the difference between the amount previously booked on a "pay-as-you-go" basis and the amount required to be booked under accrual accounting.[3] Like all price cap carriers, BellSouth will experience both of these impacts when it adopts SFAS-106.

Under SFAS-106, BellSouth will accrue as the cost of OPEBs in a given year the "Net Periodic Postretirement Benefit Cost", which includes the "Expected Postretirement Benefit Obligation" ("EPBO"). The EPBO is defined by SFAS-106 as:

> [T]he actuarial present value as of a particular date of the benefits expected to be paid to or for

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[3]See, In the Matter of Southwestern Bell and GTE Service Corp., 6 FCC Rcd 7560 (1991).

an employee, the employee's beneficiaries, and any covered dependents pursuant to the terms of the postretirement benefit plan.

The Net Periodic Postretirement Benefit Cost also includes the "Amortization of the Transition Obligation", which relates to that portion of the EPBO which has been earned, but not recognized, as of the date of adoption of SFAS-106. SFAS-106 permits companies to recognize the transition obligation on a flash-cut basis or to amortize the obligation over the average remaining service period of active plan participants.[4] Companies must also accrue interest on the entire OPEB obligation. Accrued costs are reduced by the actual return on qualified plan assets.

On December 26, 1991 the Common Carrier Bureau authorized the adoption of SFAS-106 on or before January 1, 1993 by carriers subject to the Commission's jurisdiction.[5] This ruling is consistent with Section 32.16 of the Commission's Rules[6], and with the Commission's prior

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[4]SFAS-106, paras. 112-113. If the average remaining service life is less than 20 years, a company may use a 20-year amortization.

[5]In the Matter of Southwestern Bell and GTE Service Corp. 6 FCC Rcd 7560 (1991). On May 4, 1992, the Commission released RAO Letter 20 ordering uniform accounting treatment for OPEBs.

[6]Section 32.16(a) of the Commission's Rules provides: "The company's records and accounts shall be adjusted to apply new accounting standards prescribed by the Financial Accounting Standards Board or successor authoritative accounting standard-setting groups, in a manner consistent with generally accepted accounting principles. Commission approval of a change in accounting standard will

(continued...)

determination to incorporate changes in Generally Accepted Accounting Principles ("GAAP") into Part 32 of the Rules unless the Commission decides that regulatory considerations dictate otherwise.[7] The Bureau also ordered the carriers "to defer and amortize the embedded liability in accordance with SFAS-106."[8]

The OIS raises the issue of whether local exchange carriers ("LECs") subject to price cap regulation should treat the incremental costs associated with the adoption of SFAS-106 as "exogenous" for ratemaking purposes. Each price cap LEC, including carriers such as BellSouth that have not yet adopted SFAS-106[9], was ordered to file a Direct Case setting forth its proposed treatment of SFAS-106 and responding to issues designated for investigation in the OIS.

The OIS instructs those parties required to file a Direct Case to address specific issues and to provide

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[6](...continued) automatically take effect 90 days after the company informs this Commission of its intention to follow the new standard, unless the Commission notifies the company to the contrary."

[7]Revisions of USOA for Telephone Companies to Accommodate GAAP, 102 FCC 2d 964 (1985).

[8]In the Matter of Southwestern Bell and GTE Service Corp., 6 FCC Rcd 7560 (1991). See, also RAO Letter 20, released May 4, 1992.

[9]Price cap carriers that have not yet filed tariffs implementing SFAS-106, such as BellSouth, were required by the Commission to "submit good faith estimates" of its SFAS-106 costs. All data submitted by BellSouth in this Direct Case are in compliance with this requirement.

specific information necessary to the Commission's evaluation of the "exogenous" status of OPEBs, with direct reference to the designations used in the OIS.[10] In accordance with these instructions, BellSouth's Direct Case is set forth below.

Paragraph 10 Issues.

I. Have the LECs borne their burden of demonstrating that implementing SFAS-106 results in an exogenous cost change under the Commission's price cap rules?

"Exogenous" treatment clearly is required for the incremental cost impact of SFAS-106 on price cap LECs. As demonstrated below, SFAS-106 meets the Commission's definition of an "exogenous" cost. Furthermore, SFAS-106 will impact the cost structure of price cap LECs to a far greater degree than it will impact the economy as a whole. Therefore, SFAS-106 costs will impact the GNP-PI to only a minuscule degree, and recognition of LEC SFAS-106 costs as "exogenous" in the price cap indices will not result in "double counting".

In the AT&T Price Cap Order[11], the Commission defined "exogenous costs" as "costs which change due to changes in laws, regulations, or rules, or due to other administrative, legislative, or judicial changes beyond a carrier's

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[10] OIS at para. 17.

[11] In the Matter of Policy and Rules Concerning Rates for Dominant Carriers, 4 FCC Rcd 2873 (1989) ("AT&T Price Cap Order").

control."[12] The Commission expressly recognized that changes in GAAP adopted by the FASB can give rise to exogenous cost adjustments.[13] With regard to OPEBs, the Commission has required local exchange carriers to adopt SFAS-106 accounting on or before January 1, 1993, and has ordered mandatory amortization of the transition obligation.[14] The Commission has expressly recognized that OPEBs qualify for exogenous treatment once the accounting change is mandated by the FASB and authorized by the Commission.[15]

In the LEC Price Cap Reconsideration Order[16], the Commission stated:

> [N]o carrier could treat GAAP changes as exogenous until we approved the change, and ... exogenous

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[12]Id. at para. 253.

[13]Id. at para. 295. As stated in footnote 605: "Therefore we conclude that all accounting changes imposed by outside regulatory authority can give rise to exogenous cost adjustments." See also In the Matter of Policy and Rules Concerning Rates for Dominant Carriers, 5 FCC Rcd 6786, 6807 (1990) ("LEC Price Cap Order").

[14]In the Matter of Southwestern Bell and GTE Service Corp., 6 FCC Rcd 7560 (1991).

[15]In the Matter of American Telephone and Telegraph Company, Transmittal No. 2304, 5 FCC Rcd 3680 (1990). In paragraph 4 of that order, the Commission stated: "[SFAS-106] will probably be mandated by FASB in 1992, and at that time qualify for exogenous treatment....[E]xogenous costs can be either cost changes resulting from a change in accounting rules or in any Commission-approved changes in GAAP."

[16]Policy and Rules Concerning Rates for Dominant Carriers, 6 FCC Rcd 2637 (1991), ("LEC Price Cap Reconsideration Order").

> treatment would not be granted until FASB had actually approved a change in GAAP, and the change became effective.... Further, the test of whether to grant exogenous treatment of GAAP changes is not restricted to whether the change is outside the control of the carrier.... [T]he determination of whether a particular GAAP change is exogenous includes an analysis of whether the cost change will be reflected in the inflation variable in the PCI. If a GAAP change is universal enough to be reflected in the inflation measure, exogenous cost treatment would result in double counting within the context of the PCI.[17]

The adoption of SFAS-106 is mandatory for BellSouth. Under the Commission's price cap orders and rules, the incremental impact of SFAS-106 on BellSouth's costs clearly qualifies for "exogenous" treatment in the price cap index.[18]

In order to quantify the impact of adoption of SFAS-106 on local exchange carriers, the United States Telephone Association commissioned Godwins, Inc. to prepare an analysis of the impact of SFAS-106 on the GNP-PI.[19] The Godwins' study is attached as Appendix 1. The Godwins' study demonstrates that the increase in the GNP-PI caused by SFAS-106 ultimately will provide for recovery of 0.7 percent of the additional costs incurred by price cap LECs. The study anticipates that other macroeconomic factors, such as the eventual adjustment of the national economic wage rate,

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[17] Id. at paras. 59, 63; OIS at para. 6.

[18] 47 C.F.R. Sec. 61.45(d).

[19] The Commission has recognized that to some extent changes in GAAP may be reflected in the GNP-PI. See, AT&T Price Cap Order, supra, at footnote 605.

will permit recovery of an additional 14.5 percent of the additional costs incurred by price cap LECs. Since the full impact of these macroeconomic changes will not be realized for some time, a price cap LEC that seeks exogenous treatment for only 84.8 percent of the incremental impact of SFAS-106 is employing an extremely conservative convention that will clearly understate the impact of the adoption of SFAS-106 in 1993, and no double counting will result.

II. If these cost changes are treated as exogenous,
(a) Should costs associated with implementation of SFAS-106 prior to January 1, 1993 (when the accounting change becomes mandatory) be treated as exogenous?

BellSouth currently expects to adopt SFAS-106 to become effective on January 1, 1993. Accordingly, BellSouth expresses no opinion on this issue at this time.

(b) Are the assumptions made by the individual LECs in calculating these costs reasonable?

All assumptions underlying the data submitted herein are in response to the Commission's request for a current, good faith estimate of the impact of SFAS-106 on BellSouth. The assumptions included herein are good faith actuarial estimates based on BellSouth's actual experience, and are reasonable. BellSouth's assumptions used to calculate the impact of SFAS-106 are set forth in detail below.

(c) Given these assumptions, have the individual LECs correctly computed the exogenous cost changes?

The exogenous cost calculations contained in this

Direct Case are based on current, good faith estimates of the impact of SFAS-106 on BellSouth in 1993. The estimates were made in conformance with SFAS-106 and the Commission's price cap rules, and represent BellSouth's current best estimate of the impact of SFAS-106 adoption.

> (d) Are the individual LEC allocations of these costs among the price cap baskets consistent with the Commission's Rules?

BellSouth's method of allocating these costs among the price cap baskets is in full compliance with the Commission's Rules. BellSouth based its allocation of SFAS-106 costs to the various price cap baskets on Section 61.45(d) of the Commission's Rules, which requires exogenous cost changes to be allocated on a "cost-causative basis" to price cap services and baskets. BellSouth allocated the incremental cost of SFAS-106 to the price cap baskets in accordance with Part 69 of the Commission's Rules. See Paragraph 11 (3) discussion, below.

<u>Paragraph 11 information.</u>

> At a minimum, the following information should be provided in the LECs' direct cases: (1) the date the LEC has implemented or intends to implement SFAS-106;

BellSouth's tentative plans are to adopt SFAS-106 to be effective on January 1, 1993. However, decisions relative to the adoption of SFAS-106 are still under discussion and are subject to change.

(2) the costs by year;

Under the current plan provisions the incremental interstate impact of SFAS-106 adoption on BellSouth is estimated at $887,000 for 1993. The development of these estimates is shown in Appendix 2. These estimates are based on BellSouth's current actuarial assumptions and current level of benefits. Both are subject to change.

(3) the allocation of costs to baskets by year;

The OPEB exogenous cost change was developed by determining the incremental costs resulting from the new SFAS-106 accounting standard versus the current accounting methodology. BellSouth's current methodology includes funding a VEBA trust and a "pay-as-you-go" approach. The incremental costs were developed for 1993 on an annual basis and were then applied to actual 1991 base period cost data to calculate the exogenous cost change. Part 36 Rules were used to determine interstate costs and Part 69 Rules were used to assign the costs among the price cap baskets costs of excluded services were removed from each price cap basket. To consider only that portion of SFAS-106 costs that will not be reflected in the GNP-PI (as per the Godwins' study), the amount assigned to each price cap basket was reduced to 84.8 percent of the calculated amount. Attached in Appendix 3 is a summary of BellSouth's OPEB exogenous cost change, which also includes the assignment to price cap baskets.

(4) the treatment of these costs in reports to the Securities and Exchange Commission (SEC) and to shareholders, including specific citation to, or excerpted materials from, such reports;

The financial statement disclosures in BellSouth's 1991 Annual Report relative to OPEBs are attached as Appendix 4. These disclosures were included in the 10-K by incorporation.

> (5) all studies on which the LEC seeks to rely in its demonstration that these accounting changes should be considered exogenous cost changes, including all studies demonstrating that the change is not reflected in the current price cap formulas, factors for inflation, productivity, allowed exogenous changes, initial price cap rates, and the sharing and low-end formula adjustment mechanisms.

BellSouth relies upon the Godwins' study included in Appendix 1 to this filing. BST is only requesting exogenous treatment of the incremental postretirement expenses that will not be reflected in the GNP-PI (84.8% of the total incremental amount). These incremental costs have not been included in prior rates. Because, these prior rates were used to determine the productivity factor assigned by the Commission, the incremental impact is not included in the productivity factor. Similarly, the incremental cost could not have been included in the sharing and low-end adjustment marks.

<u>Paragraph 12 information.</u>

Paragraph 12 does not request any specific information from BellSouth.

<u>Paragraph 13 information.</u>

> In particular, the LECs should describe:
> (1) each of the type of benefits being provided that is covered by the SFAS-106 accounting rules;

BellSouth offers the following OPEBs to its employees:

Medical Assistance Plan (MAP) including Medicare Part B. See Summary Plan Description attached as Appendix 5 to this filing.

Dental Assistance Plan. See Summary Plan Description attached as Appendix 6 to this filing.

Group Life Insurance. See Summary Plan Description attached as Appendix 7 to this filing.

(2) for 1991 and 1992, the pay-as-you-go level of expenses associated with these benefits;

BellSouth's total medical/dental/life "pay-as-you-go" amounts are \$138.3 million for 1991. The estimated amount for 1992 is \$149.5 million. These amounts represent total claims paid to BST retirees for each of the years indicated. Since the majority of the claims paid to retirees are paid from the VEBA trusts, an interstate component of claims paid is not appropriate. See the response to paragraphs 11 (2) and 13 (4) for a description of BellSouth's method of expensing.

BellSouth's total postretirement expenses for 1991 and 1992 are as follows:

	1991 Actuals	1992 Estimates
VEBA Trust Contributions	$142.4	$157.5
"Pay-as-you-go" (pre 5/1/85 retirees)[20]	38.8	46.5
Total BellSouth Postretirement Costs	181.2	204.0

(3) any Voluntary Employee Benefit Association (VEBA) trusts or other funding mechanisms for these expenses which were established prior to the adoption of SFAS-106;

During 1989 and before, all health postretirement funding was made to a single VEBA trust developed under Internal Revenue Code Section 501(c)(9). The amounts funded are applicable for the cost of projected future benefits for employees that retired on, or will retire after, May 1, 1985.

In 1990, a second health trust was formed as a result of the 1989 Collective Bargaining Agreement ("Collective Bargaining Trust" or "CBT"). The cost of projected future benefits for all active employees covered by the Collective Bargaining Agreement are being funded into the CBT. When the CBT was formed, it was designated as being for the benefit of all collectively bargained employees, and the original trust was designated for management employees and other non-representable employees that retired on, or will retire after, May 1, 1985. The CBT was also formed under Internal Revenue Code Section 501(c)(9).

[20]The "pay-as-you-go" amounts in 1991 and 1992 are more than those projected for 1993 (See, Appendix 2) because the caps that were bargained for in 1989 become effective in 1993.

In 1988, a life trust was formed, in addition to the retiree life revenue account that had existed, to fund the cost of life claims for eligible employees. All employees that are covered by the pension plan are eligible for life benefits. The life trust was also formed under Internal Revenue Code Section 501(c)(9).

(4) the forms of postretirement benefit accrual accounting, if any, that were adopted within the regulated financial reporting before the adoption of price cap regulation;

In addition to the "pay-as-you-go" amounts expensed, BellSouth also expenses its contributions to the VEBA trusts described above. The contributions to the trusts are actuarially determined amounts that are calculated in accordance with IRS tax codes and are made pursuant to ERISA requirements.

(5) what type and level of SFAS-106-type expense is reflected in current rates; and
(6) what type and level of SFAS-106-type expense was reflected in the starting rates for price caps.

BellSouth has a combination of contributions to the VEBA trusts (to partially fund benefits of current and future retirees), and "pay-as-you-go" amounts reflected in the prospective costs that underlie its initial price cap rates. The contributions to the trusts included amounts funded for all representable employees as well as amounts funded for management and non-representable employees retiring after May 1, 1985. In addition, BellSouth included "pay-as-you-go" amounts for management and non-representable employees that retired before May 1, 1985. No additional "SFAS-106-type" (postretirement) expenses were included in the initial or current price cap rates.

Paragraph 14 information.

> We also seek descriptions and justifications of the actuarial assumptions, and the assumptions unique to postretirement health care benefits, made in computing the SFAS-106 expenses. These assumptions should include, but are not limited to, the time value of money, participation rates, retirement age, per capital claims cost by age, health care cost trend rates, Medicare reimbursement rates, salary progression (if a company has a pay-related plan), and the probability of payment (turnover, dependency status, mortality, etc.). Parties and commenters should also discuss what assumptions, if any, were made about future events such as capping or elimination of benefits, or the possible advent of national health insurance.

BellSouth made the following actuarial assumptions in computing its currently estimated SFAS-106 expenses for both its medical/dental plan and its group life plan (which are subject to change):

Return on Assets: 8.00 percent compounded annually. This rate was developed in compliance with the provisions of SFAS-106. In selecting this rate, consideration was given to returns being earned on BellSouth's currently invested plan assets as well as rates of return expected to be available for reinvestment.

Discount Rate: 9.00 percent compounded annually. In selecting this rate, consideration was given to the return on high-quality fixed income investments currently available which have cash flows that match the timing and amount of

BellSouth's expected benefit payments, as required by SFAS-106.

Participation Rates: BellSouth does not have a contributory plan. Consequently, 100 percent of eligible employees participate.

Retirement Age: Actuarially determined normal retirement age is 55 and is based on BellSouth's experience from 1975 through 1985, as modified in 1991 to reflect plan amendments adopted after 1985 that provide incentive for postponing election of service retirements.

Claims Cost: Claims costs are based on the latest available retiree-specific historic enrollment and claim payment data. Actual claims data from 1988 through 1990 were used to forecast an average base for medical claims incurred in 1991. The average claim cost includes dependent coverage. The average monthly claim cost is as follows:

Medical

Management employee under 65	$395.00
Management employee over 65	136.00
Non-Management employee under 65	385.00
Non-Management employee over 65	113.00

Dental

Management employee	$ 29.00
Non-Management employee	14.20

Health Care Cost Trend Rate: Dental trend is assumed to start at 6 percent per year in 1990 and grade down to 3 percent for 1996 and after. Since the rate of increase is not assumed to be age-sensitive, no adjustment is required for the aging of the retired group.

Medical trend, which includes medical care utilization and the effect of aging of the population, is assumed to range from 11 percent in 1993 to a high of 13 percent in 1995 and then declines to 7 percent in the year 2007 for employees under age 65. For employees over age 65, medical trend ranges from 4 percent in 1993, to a high of 5.2 percent in 1995, declines to 5 percent in 1996 and stays constant thereafter. It is further assumed that 1 percent of such trend results from population aging. The medical growth assumption discussed above is consistent with health care costs in the economy, and levels off at 25 percent of the GNP.

Both the medical and dental trend rates were developed using BellSouth's actual experience from July, 1988 through December, 1990.

Medicare Reimbursement Rates: Effective January 1, 1990, BellSouth's reimbursements to present and future service and disability retirees and/or Medicare-eligible spouses of service and disability retirees will be frozen at 1990 levels, excluding the premiums associated with the catastrophic coverage provisions of the Medicare Program. Also, MAP will continue to be secondary to Medicare for those eligible for coverage regardless of their enrollment status.

Salary Progression: BellSouth's medical and dental plans are not salary related. Therefore, this question is not applicable for those plans. Salary progression for the life plan is based on salary at retirement. Salary at retirement is projected using salary scale projections.

Turnover: Separation rates were derived from a study of the experience of BellSouth management and non-management employees for the period 1975-1985.

Dependency status: Dependents of living retirees are covered under the plan except as noted under "Capping Assumptions" below. Surviving dependents have 6 months of coverage at company expenses and then can continue coverage at their own expense.

Mortality: Preretirement and postretirement rates were derived from a study of the experience of BellSouth management and non-management employees for the period 1980-1985 for active employees and 1976-1983 for retirees.

Termination Rates: Annual rates of employment separation were derived from a study of the experience of BellSouth management and non-management employees for the period 1975-1985.

Capping Assumptions: As a result of 1989 bargaining, BellSouth's contributions for postretirement medical and dental contributions were frozen at 1990 actual cost levels for anyone eligible for postretirement benefits as a result of being eligible for a service or disability pension, whose pension effective date is on or after January 1, 1992. The excess amount of the Plan's medical and dental cost (claims and administrative cost) above the Plan's 1990 cost (the company's frozen contribution level) is to be deducted from pension payments as an average premium cost, based on the total retiree cost experience beginning on January 1, 1993. Subsequent yearly participant contribution requirements (for example, in 1994, 1995, etc.) will be the amount that the Plan's cost, two years in arrears of the effective date of the revised contributions, exceeds the actual retiree cost in aggregate for the Plan's 1990 cost (the Company's frozen contribution amount).

In addition, as a result of 1986 bargaining, eligibility rules for employees whose term of employment is less than 30 years that retire (in other than a special early out program) on a service or disability pension on or after January 1, 1988, were revised to require payment of an equivalent premium for a portion of their health care benefits. Eligibility rules for employees who retire on a service or disability pension on or after January 1, 1988, were revised to exclude Company-paid coverage for dependents, other than spouses, acquired after retirement. Retirees may pay the full cost premiums for coverage for any otherwise eligible acquired dependents.

BellSouth made no assumptions regarding elimination of benefits or the possible advent of national health insurance. BellSouth's actuarial assumptions include a leveling of health care costs, but does not assume any specific cause of such cost leveling.

Paragraph 15 information.

> Further, since part of the growth in the GNP-PI presumably occurs due to growth in medical costs, we seek information on what adjustment, if any, should be made in the exogenous adjustment to avoid any double counting. If an adjustment has been made, parties and commenters should document how the adjustment was computed. Moreover, parties and commenters should describe and quantify any wage changes which will be reflected in the GNP-PI that are expected to occur as a result of the introduction of SFAS-106. In particular, parties and commenters should discuss what adjustment, if any, should be reflected in the exogenous adjustment for this change.

No adjustment is necessary. The change in accounting that requires exogenous cost treatment reflects the incremental difference between the amount of postretirement expenses the LECs are currently recovering and the amount that will be incurred under SFAS-106. Since both the current postretirement expenses and the SFAS-106 expenses have growth embedded in them, the incremental difference for which the LECs' are seeking exogenous treatment does not include an additional growth factor. Consequently, there is no double counting with respect to growth.

The impact of SFAS-106 on future wages was taken into account in the Godwins' study. That study demonstrated that only 0.7 percent of the average cost increase experienced by a price cap LEC will be reflected in the GNP-PI. The Godwins macroeconomic model estimates that national wage rates could eventually decline such that 14.5 percent of the additional SFAS-106 costs would be recovered. Since this possible recovery will be realized only over time, if at all, a LEC that seeks recovery of only 84.8 percent of its incremental SFAS-106 costs in 1993 is employing an extremely conservative convention.

Paragraph 16 information.

> Finally, parties and commenters relying on the macroeconomic model used in the USTA study should fully describe and document the model, including the method of estimation, parameter estimates, and summary statistics. This same data should be submitted for any alternate functional forms which were modeled, including the data used to estimate the model, the data used in making forecasts from the model, and the results of any sensitivity analyses performed to determine the effect of using different assumptions.

Godwins has developed a detailed response to the request for information contained in Paragraph 16 of the OIS. BellSouth has included the Godwins' response as Appendix 8.

For the reasons set forth above, BellSouth respectfully submits that exogenous cost treatment of the incremental impact of SFAS-106 no later than January 1, 1993 is appropriate.

Respectfully submitted,

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